BlackRock.

18th December 2024

HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Submitted via email to: FSGrowthStrategy@hmtreasury.gov.uk

RE: Financial Services Growth & Competitiveness Strategy Call for Evidence

BlackRock[1] is pleased to have the opportunity to respond to the Financial Services Growth & Competitiveness Strategy Call for Evidence, issued by HM Treasury (HMT).

BlackRock supports a regulatory regime that increases transparency, protects investors, and facilitates responsible growth of capital markets while preserving consumer choice and assessing benefits versus implementation costs.

We welcome the opportunity to comment on the issues raised by this Call for Evidence and will continue to contribute to the thinking of HMT on any issues that may assist in the final outcome.

We welcome further discussion on any of the points that we have raised.

Yours faithfully,

Antony Manchester
Co-head of Government Affairs and
Public Policy, EMEA
antony.manchester@blackrock.com

[1] BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers and other financial institutions, as well as individuals around the world.

BlackRock

Executive summary

As BlackRock's Chairman and CEO, Larry Fink, set out earlier this year, we believe the growth- and prosperity-generating power of the capital markets will remain a dominant economic trend through the rest of the 21st Century.[2]

The Financial Services and Markets Act (FSMA) 2023 gives the UK a regulatory framework with objectives where consumer protection, market integrity and financial stability remain paramount; alongside the ability to develop smarter regulation, expand the UK's capital markets, and grow the number of individuals participating in – and benefitting from – financial markets.

Indeed, we believe it is critical that regulation be designed in a way that not only protects those who already use financial services, but also considers the impact it can have on financial inclusion and well-being by promoting regulation which expands the number of people saving and investing, and the range of services available to them.

As the Government develops its strategy for financial services growth and competitiveness, we recommend prioritising the following areas:

Democratising investment: Encouraging more people to start investing could be transformative for their financial wellbeing, while also spurring growth of the UK's capital markets. This can be done by:

- Using the ongoing review of the Advice / Guidance boundary to develop 'Targeted Support' offerings that nudge and steer customers towards appropriate financial products.
- Simplifying retail disclosures, and re-contextualising investment risk warnings to help individuals make an informed decision about the risk and reward trade-off involved with investing, and how it fits with their wider financial goals – recognising the benefits of investing as well as the potential risks.
- Facilitating access to low-cost investment options, drawing inspiration from the success of Exchange Trade Fund (ETF) savings plans in Continental Europe.
- Expanding retail access to alternative investments by making the Long-term Asset Fund (LTAF) eligible for the Stocks and Shares ISA; and continuing to refine the LTAF framework to ensure it is fit for purpose in the Wealth market.

Financing the transition: We believe the UK's approach to the regulation of sustainable finance is well-developed. Following several iterations of the UK's Green Finance Strategy, a significant amount of work has been completed on 'greening finance' in the UK. This will be complemented by plans to implement internationally-aligned corporate reporting standards, and consider the role of corporate transition plans.

[2] Larry Fink's 2024 Annual Chairman's Letter to Investors

In the UK, policymakers have identified a particular need to increase development of energy infrastructure, to meet both the demands of the transition to a low-carbon economy and to enhance the country's energy security. We believe this can be delivered through:

- Co-investment with the private sector, where needed, to attract internationally mobile capital looking for such opportunities. Public-private co-investment can offset risks involved in infrastructure projects, which are particularly acute where technologies or business models are not proven, and where the UK is competing with initiatives in other countries chasing the same funding.

- Developing a pro-investment regulatory regime: Operators of infrastructure assets are often subject to stringent regulatory regimes, which influence business models and finance-raising decisions. Regulators need clear mandates on their role and responsibilities in facilitating infrastructure projects and investment.

- A supportive planning framework: Timelines for planning approval influence the economic viability of projects, and uncertainty over whether and when approvals will be received generate risks that businesses and investors cannot price, deterring investment. The ongoing review of the UK's planning framework and Nationally Significant Infrastructure Projects regimes provides an opportunity to shorten planning timelines.

A balanced regulatory environment: The political independence, expertise and quality of the UK's regulators underpins the competitiveness and reputation of the UK financial services industry. Government and regulators must continue to ensure that regulatory objectives set out in the Financial Services and Markets Act 2023 are appropriately balanced. Areas that warrant greater focus include:

- Revising His Majesty's Revenue and Customs' (HMRC) restrictive approach to the available Value Added Tax (VAT) exemptions which apply to the UK funds industry. This has the potential to significantly increase the costs borne by retail investors.

- Introducing a zero rate of VAT for investment management services would reduce the tax levied on retail investors when accessing collective investment vehicles and strengthen the competitiveness of the UK as a hub for international asset management. Where VAT is charged, this represents an explicit tax cost to the investors in the fund.

- Reforming the Financial Services Compensation Scheme (FSCS) in line with the 'polluter pays' principle, to ensure that the costs of compensation are internalised by the sectors that generate them.

- Further review of the Solvency UK regime for insurers to identify additional ideas that can advance the UK's objectives on growth and competitiveness. For example, Pheonix Group have proposed a Matching Adjustment (MA) 'Sandbox' that would allow insurers and the PRA to potentially expand the range of assets insurers are able to invest in.

Promoting financial services across the country: International organizations give consideration to a wide range of factors when making decisions on where to set up operations. This includes the regulatory and legal environment, access to talent, local infrastructure and amenities, and the ability to connect with clients and conduct cross-border business.

Facilitating technology and innovation: Adoption of new technologies relies on several factors. While regulation is important, so too is the ability to create a network effect. This requires scalable Financial Market Infrastructure that brings together market participants across the full financial spectrum and allows them to seamlessly interoperate. One way to do this is to identify and remove existing structural micro barriers to entry – for example:

- Expanding the pool of eligible collateral acceptable to market participants to certain Money Market Funds and Exchange Traded Funds could subsequently allow units of these funds to be tokenised. Asset owners would then benefit from new forms of digital asset utility, operational efficiencies and potential commercial opportunities arising from new tokenised fund distribution networks, thereby increasing network participation.

Supporting the UK FinTech sector: The UK FinTech sector can be supported through use of regulatory sandboxes, tailored regulations for emerging technologies, and streamlined licensing processes for FinTech startups.

Vibrant listed equity markets: Public equity markets are a critical part of a well-functioning capital markets ecosystem. Recent reform to the listings regime and public equity market in the UK can be bolstered through:

- Stamp Duty reform: The UK's Stamp Duty Reserve Tax is the highest tax-on-shares in the world. This serves as a deterrent to retail investors and pension funds investing more in the UK. An incremental reduction could first reduce the tax for some priority subsectors, before considering a broader-based reduction.

- Development of a consolidated tape for equities and ETFs: The EU is moving at pace to deliver its framework for a Consolidated Tape for both bonds and equities; and the US stock market has had an equities tape since 1975 and a bond tape for over 20 years. We believe the UK needs to accelerate its progress to maintain its position as a modern capital market.

Democratising investment

Barclays estimates that there are 13 million people holding £430 billion of cash savings which could be suitable for investment.[3] Encouraging more people to start investing could be transformative for the financial wellbeing of people across the UK, while also spurring growth of the UK's capital markets. However, there can be a perception that investing is highly risky and only for the wealthiest in society.

There is also a significant gender gap in the UK when it comes to retail investing: research conducted by the Investment Association finds that 63% of all retail investors are male.[4] In our view, a major driver for this is appetite for risk (real or perceived), and confidence in investing. Tackling this issue, and encouraging more women to invest, should be a major priority for this Government.

Outlined below are some ways barriers that prevent uptake to retail investing can be addressed.

Closing the advice gap

We strongly support ongoing work by the FCA and HMT to close the advice gap. We are highly supportive of the objectives of the Targeted Support framework proposed by the FCA, which will enable firms to nudge and steer customers towards better behaviours and outcomes. This will allow more people to participate in financial markets, with the confidence of appropriate support. If aligned with other strategic policy changes, such as the overhaul of the disclosures regime, we could see a material improvement in the decisions consumers make and the value and wealth they are consequentially able to derive.

Improved disclosures and risk warnings

It is well recognised that existing consumer investment disclosures are complex, and not well suited for the purpose of empowering investors to make informed investment decisions. Research by Barclays suggests individuals can overestimate the risk of losing money from investing, even over long-term time horizons, compared to historical performance.[5]

We welcome the FCA's ongoing work to simplify disclosure messages and processes, and ask that the focus of the upcoming consultation on the new Consumer Composite Investments (CCIs) regime remains on ensuring that individuals receive the information they need in a clear and understandable format. This includes, for instance, amending risk warnings to help individuals make informed decisions about the risk and reward trade-off involved with investing, and how it fits with their wider financial goals. Disclosures should recognise the benefits of investing, not just the risks – providing balanced, contextualised information.

In order to most efficiently support retail investors in their financial decision making, it is also important that disclosures are assessed within the broader context of the entire distribution chain. This means not only tackling complexities created by the inherited PRIIPs disclosure regime, but also ensuring alignment in the CCI's interaction with the Markets in Financial Instruments Directive (MiFID II), the Insurance Distribution

[3] Barclays, *Empowering retail savers to engage with investing: the role of public policy*, September 2024. Figures are based on savers who hold more than six months' income in cash savings.
[4] The Investment Association, *Investment Management in the UK 2023-2024*, September 2024
[5] Barclays: *The UK investment gap: £430 billion in cash savings not invested by UK adults*, September 2024

Directive (IDD) and the Advice / Guidance boundary – particularly given this will impact a broad set of consumers, including those who are decumulating their pension assets – to ensure that the goals of simplification, clarity of understanding and ease of access are most effectively addressed.

Facilitating access to low-cost investment options

Exchange-traded funds (ETFs) have seen significant growth globally, providing simple and low-cost access to financial markets. While the UK has a large institutional ETF market, relative to other regions like the US or Continental Europe – and in particular Germany – adoption of ETFs among retail investors is low.

Indeed, individual ETF saving plans have gained in significant popularity in Europe. The number of ETF plans executed per month in Continental Europe rose 42% to 10.8 million in 2024, compared to 7.6 million in 2023. Several factors have underpinned this growth, but perhaps the most significant fact is the ability to invest small regular amounts, sometimes as little as one Euro. ETF savings plans have also made investing more accessible to a broader audience, reflected in the fact that a younger demographic (those aged 18 to 34) is the most active in investing in ETFs. Further to this, in Germany, women are expected to make up 48% of new ETF investors over the next 12 months.[6]

We believe growth of retail ETF investing in the UK is constrained by the current market structure for execution of retail trade orders, where there is limited choice of execution venues, creating an uneven playing field versus more sophisticated or institutional market participants, and resulting in lower execution quality. There is also a lack of protection against sub-optimal execution outcomes during heightened market volatility, compared to market participants that are able to utilise centralised order book trading on exchanges. This includes a lack of guaranteed execution by Retail Service Providers (RSPs), instances of which are particularly high in fast-moving markets, and absence of volatility safeguards which exist on exchanges. We also see limited transparency in consolidated transactions data (i.e. the lack of a consolidated tape), costs & charges levied during order intermediation, and limited disclosure requirements on order execution quality.

Further take-up could be improved by:

- *Improving competition, order handling, and reporting practises for retail orders:* Currently, the RSP model facilitates single-execution and single-settlement of retail orders by the chosen RSP on a bilateral agency basis. While retail trades are reported on the London Stock Exchange ex-post, they do not necessarily benefit from access to LSE's (or other exchanges') order book whereby orders interact with market-wide liquidity. Retail orders executed via the RSP model are also marked as 'Off Order Book – On Exchange' which leads retail investors to believe their orders have been executed on exchange, which may not necessarily be the case. Retail investors should be given the option to choose whether their orders are executed on an exchange or the RSP network, with clear disclosures about the actual execution venue.

- *Implementing volatility guardrails for retail orders:* Trades executed on-exchange benefit from safeguards during periods of heightened market volatility. Under the RSP model, these are not currently available. To enhance

[6] BlackRock: *The ETF savings plan study 2024*

the resiliency and fairness of retail order execution at the time of heightened market volatility, we recommend taking steps to ensure RSPs implement similar controls.

- *Delivering a consolidated tape and transparency on intermediation costs:* A single consolidated tape provider of pre- and post-trade data (see 'Vibrant listed equity markets' section, below) will allow executions via the RSP process to be benchmarked against the wider market, driving best execution and better outcomes. We also recommend exploring ways to improve transparency of costs and other charges levied by different service providers throughout retail investment process, from order placement on a brokerage platform to its execution and settlement.

Access to alternative investments

As the size of – and investor interest in – private markets continues to grow, we believe there is the opportunity for the UK to cement its leadership in innovative fund structures like the Long-Term Asset Fund (LTAF). While there has been significant growth and interest in the LTAF for pensions, there has been less uptake by retail investors.

In the mass retail market, we would stress the need to meet retail investors where they are, and allow the LTAF in the Stocks & Shares ISA, rather than just the Innovative Finance ISA. Given the relative size of and inflows to the two wrappers, doing so would help build the scale needed and would benefit retail investors by granting them access to a broader range of investment strategies.[7]

More broadly, we see two factors holding the LTAF back from further adoption in the wealth market. Firstly, the three-month redemption period can be a barrier for some wealth management firms – and we note the update to the European Long-Term Investment Fund (ELTIF) framework now allows for more frequent redemption and/or shorter notice period under certain conditions (having liquid assets or setting redemption maximums). Building this type of flexibility into the LTAF may make it more attractive to wealth investors. Secondly, a lack of UCITS eligibility can also act as a barrier to further adoption.

Financing the transition

We believe the UK's approach to regulation of sustainable finance is well-developed. Following several iterations of the UK's Green Finance Strategy, a significant amount of work has been completed on 'greening finance' in the UK. This will be complemented by plans to implement internationally-aligned corporate reporting standards, and consider the role of corporate transition plans.

The transition to a low-carbon economy is, as noted above, one of several forces re-shaping financial markets. The transition isn't a single trend – it is a multifaceted process. Investing in the transition, in our view, encompasses investing with a focus on preparing for, being aligned to, benefitting from, and / or contributing to the transition to a low-carbon economy.[8]

[7] Only £144m was held in Innovative Finance ISAs across 17,000 accounts in the 2021/22 tax year. Comparatively, more than £34bn was held in Stocks & Shares ISA during the equivalent period.
[8] See BlackRock, *Sustainable and transition investing*

Preparing for the transition includes investing in operational improvements or assets better positioned for the transition. Being aligned to the transition would include investing in portfolios or assets on a generally accepted low carbon pathway. Benefitting from the transition would include investing in assets that provide key inputs necessary for the transition. Contributing to the transition would include investing in assets required to mitigate real-world emissions

None of these areas are mutually exclusive. Activities within any of the categories could be both enablers of the transition, or actively drive the transition. And policy can help encourage each of these areas in different ways.

The UK has already brought in policy that ensures investment products and services are accurately described: for example, the FCA's recently agreed Sustainability Disclosure Regulation (SDR) framework and anti-greenwashing rules for investment funds look to ensure 'truth to label' in marketing of products that have investment objectives relevant to different aspects of investing in the transition.

Beyond this, robust disclosure by companies is essential for investors to effectively evaluate companies' strategy and business practices related to material sustainability-related risks and opportunities. The International Sustainability Standards Board (ISSB) standards, IFRS S1 and S2, provide companies with a useful guide to preparing disclosures that can support investors' ability to make these assessments. We welcome the government's intention to consult on the introduction of these standards for 'economically significant' companies in the UK.

Corporate transition plans can be complementary to these disclosures. Transition plans, in our view, are a method for a company to both internally assess and externally communicate long-term strategy, ambition, objectives, and actions to create financial value through the global transition towards a low-carbon economy. Investors can use this information to make more informed decisions. We note that ISSB is beginning to build on the work of the UK Transition Plan Taskforce to drive further harmonisation of sustainability reporting. We understand the government will also consult on how any transition plan framework will be implemented in the UK.

Beyond this, government can play an important role in enabling investments that will contribute to the low-carbon transition. In the UK, policymakers have identified a particular need to increase development of energy infrastructure, to meet both the demands of the transition to a low-carbon economy and to enhance the country's energy security. Private sector investment has already played a significant role in financing the UK's infrastructure base, but meeting the ambitious targets set by the government will require further focus on getting the policy environment right to continue to attract private capital.[9]

There are several crucial factors private investors have to take into account when considering an infrastructure project: whether the design and technology underpinning the infrastructure is proven, in development, or early-stage; whether the business model of a given project or enterprise is proven; and the attractiveness of its risk-return profile – which is influenced significantly by government policy, regulation, and support mechanisms. We believe there are three major areas of policy that are important to get right if the UK is to attract private investment in infrastructure it requires.

[9] The UK's The UK's National Infrastructure Commission has commended the UK's regulatory model for infrastructure financing, noting that between 2018/19 and 2020/21 the vast majority of energy infrastructure was privately financed. See HM Treasury, *National Infrastructure Strategy: Fairer, faster, greener*, November 2020.

First, co-investment with the private sector, where needed. Public-private co-investment can offset risks involved in infrastructure projects, which are particularly acute where technologies or business models are not proven. For example, the UK's capacity in offshore wind generation – which saw 10% growth per annum between 2013 and 2023 – was supported by a PPP established in 2015 in the form of Contracts for Difference (CfDs).[10] When the offshore wind sector was still nascent, CfDs helped to provide investors more confidence in revenue streams in a market than can otherwise be volatile.

Second, developing a pro-investment regulatory regime. Operators of infrastructure assets are often subject to stringent regulatory regimes, because they provide important services to the economy and the public. In the UK, the business model of infrastructure companies – including their ability or willingness to raise financing for new developments – is shaped by sectoral regulators, who receive their mandates and objectives from the government. Indeed, in the UK, regulators have significant influence over the permitted returns on regulated assets, and their capital expenditure plans. Regulators need clear mandates on their role and responsibilities in facilitating investment in infrastructure projects, which may mean recognising that there are trade-offs between regulators' objectives, and prioritising those related to infrastructure investment.

Third, a supportive planning framework. In the UK, obtaining planning permission for infrastructure development can be a multi-year process. Timelines for planning approval influence the economic viability of projects, and uncertainty over whether and when approvals will be received generate risks that businesses and investors cannot price, deterring investment. The ongoing revisions to the UK's planning framework and Nationally Significant Infrastructure Projects regimes provides an opportunity to shorten planning timelines.

A balanced regulatory environment

We believe the political independence, expertise and quality of the UK's regulators underpins the competitiveness and reputation of the UK financial services industry.

This extends to the regulators' ability to interpret the current regulatory framework. The hierarchy of objectives set out in the Financial Services and Markets Act 2023 appropriately balances the protection of consumers, market integrity, the promotion of competition, and growth and competitiveness of the sector.

Further to this, it is important to understand what the regulators are doing well and where there is opportunity for improvement. As a result, HMT and other regulators such as (but not limited to) The Pension Regulator (TPR), Competition Market Authority (CMA) and His Majesty's Revenue and Customs (HMRC) should all be included in the discussion about growth and competitiveness. This is essential to promote collaboration across the policymaking landscape and ensure that the breadth of policy initiatives do not conflict with or offset the benefits of one another.

Separately, we welcome regulators' efforts to address the capacity constraints that exist within the FCA and PRA's product authorisation processes, and commend the adoption of digitisation to streamline this process, given the importance not to inhibit access to a wide range of products for UK investors. Overly complex, administrative, or time-consuming authorisation processes could disincentivise fund managers and

[10] For statistics on UK offshore wind generation capacity, see Energy Institute, *Statistical Review of World Energy*, 2024.

increase the time for products to get to the UK market. This could also reduce the desirability of the UK as an international financial centre and/or lead to sub-optimal outcomes for UK retail investors wanting to invest in a range of products compared to their European counterparts.

We welcome the renewed focus outlined by the Chancellor in her recent remit letters to all UK financial services regulators, emphasising the need to further embed the government's policy of competitiveness and growth within the regulatory agenda. Government and regulators must continue to ensure that regulatory objectives are appropriately balanced. We outline below some considerations for different sectors.

Cost of doing business in the UK: FSCS and VAT for investment management services

An area for improvement, in our view, relates to the Financial Services Compensation Scheme (FSCS) Framework. The FSCS, in its current form, adds to the cost of conducting financial services business in the UK. The cost of the compensation is shared by the entire industry, and does not effectively target the sectors causing the failures. Whilst we strongly agree and support consumers being protected from the potential costs of misconduct and poor advice, we are concerned that funding compensation by cross-subsidising between different sectors reduces trust and confidence in the financial services sector given that compensation is a consequence of conduct failures, and it is the fact that conduct failures have occurred that reduces consumer trust and confidence, regardless of whether compensation is ultimately paid.

We believe the FSCS should be viewed primarily as an insurance mechanism, available if firms cannot meet their own compensation liabilities. The responsibility for consumer protection and preventing failures more broadly should rest with business and regulators. As such, the compensation framework should adhere strictly to the 'polluter pays' principle and should therefore be fundamentally reformed to ensure that the costs of compensation are internalised by the sectors that generate them.

Separately, HMRC's restrictive approach towards available VAT exemptions, which apply to the UK funds industry have the potential to significantly increase the costs of operating UK funds. Any VAT that is added to fees which are currently VAT exempt will become a cost to the fund and ultimately be borne by retail investors. HMRC's current approach is increasing the uncertainty of the UK's tax system for financial services businesses and could undermine efforts to boost the attractiveness of the UK as a global investment management hub. UK funds could be at a significant economic and competitive disadvantage compared to those domiciled in other locations, where VAT exemptions for funds services remain available. In the medium to longer term, HMRC's approach may result in reduced tax revenue for the Exchequer.

A more competitive measure would be to introduce a zero rate of Value Added Tax (VAT) would reduce the tax levied on retail investors when accessing collective investment vehicles and strengthen the competitiveness of the UK as a hub for international asset management. Under the current VAT regime, management fees charged to a UK investment fund are either exempt from VAT if the fund is a qualifying fund, or subject to VAT if not. Where VAT is charged this represents an explicit tax cost to the investors in the fund. Whilst exemption removes an explicit VAT charge on the fee levied by the manager to the fund, it results in non-recoverable VAT costs within the supply chain which will form a cost component of the fee charged to the fund, and as a result, represent an implicit cost to the investor. In both scenarios, the cost for the investor is increased, either explicitly or implicitly, by VAT.

We also believe it would result in medium- to long-term fiscal benefits for the Government, as research conducted by The Investment Association (IA) indicates that a VAT zero rate for asset management is also expected to be revenue accretive for the UK, increasing over a five-year period (and then going forward in perpetuity) net tax revenues for the Exchequer[11].

Insurance & Reinsurance Markets

The UK insurance industry provides critical services to individuals and companies, as well as being major investors in the UK. Changes in funding levels for DB pension schemes also create the scope for the insurance sector to expand, through pension risk transfer arrangements.

The regulatory regime for insurers strongly influences the type of business they can write (for example, their ability to provide guaranteed products), where their capital is invested, and their ability to export services in a global, competitive market.

The regulatory regime in Europe – including the UK – is generally recognised as conservative with respect to the risk that insurers can take on, impacting the areas outlined above. We support further review of the UK's solvency regime to identify additional ideas that can advance the UK's objectives.

For example, while Solvency II/UK Matching Adjustment (MA) reform has been a positive step towards allowing insurers to invest in a wider range of assets, there is scope for continued improvement, with the objective to promote the sector's growth and competitiveness.

Insurers must seek PRA approval for each type of asset for which they propose to use the Matching Adjustment. However, the process can be onerous and time consuming, and the outcome often uncertain. Indeed, even when asset classes are approved, insurers then carefully examine the creditworthiness of each asset considered for their Matching Adjustment portfolio, even if this has been independently and thoroughly done externally. The additional layer of review makes access to certain assets challenging as the credit approval processes cannot run as quickly as the security syndication process.

Pheonix Group have proposed a MA 'Sandbox' that would allow insurers and the PRA to investigate that are currently not MA eligible, but that are i) fundamentally suitable for matching liabilities; ii) economic growth-enhancing; and iii) provide highly predictable cash flows.[12] This could be combined with further transparency on assets that have ultimately been approved by the PRA. Appropriate safeguards could be put in place to ensure financial curing of any deficiency that should arise, should assets in the sandbox not perform as expected.

We believe this could provide a way to expand the range of assets insurers can invest in, while maintaining prudential standards – consistent with the PRA's objectives under the Financial Services and Markets Act to maintain financial stability and promote growth and competitiveness.

[11] The Investment Association, *Spring Budget Submission, 2024*
[12] See Phoenix Group, *Solvency UK: the case for introducing a Matching Adjustment Sandbox*, May 2024

Promoting financial services across the country

As a global organization, when making decisions on where to locate operations, consideration is given to:

- *The regulatory and legal environment*: A robust and transparent regulatory framework is paramount and provides a stable environment for business. A well-established legal system and contract enforcement, along with regulatory bodies that uphold market integrity and investor confidence, are crucial.

- *Access to talent and employment costs*: A highly skilled and diverse talent pool, particularly in sectors like finance and technology, is essential. The presence of world-renowned universities and research institutions ensures a steady supply of qualified professionals.

- *Real estate, essential infrastructure, and amenities*: Infrastructure and development projects that enhance connectivity and business opportunities is an important consideration.

- *Connectivity to clients and conducting cross-border business*: Locations that provide easy access clients, and / to transact with other markets are beneficial.

While there are no significant barriers to creating jobs in the financial services sector outside of London, development of regional financial centres requires both the ability to attract and maintain access to a skilled talent base in addition to ensuring regional hubs are practical places to live and work, with good transport links comparable to London. Below we discuss further some of the issues that impact all sectors, reflections on the UK asset management sector, and provide a case study on Scotland's success as a centre for asset management activity.

Skills & Access to Talent

Recent surveys demonstrate that the UK continues to be a leading destination for global talent in financial services.[13] At BlackRock, we primarily use the skilled worker visa for internal mobility of overseas staff and experienced international talent. More broadly, we support immigration policy that facilitates mobility of skilled workers between financial centres and within groups. This includes mobility at more junior levels, to allow the UK to benefit from being able to recruit and retain talent from as wide a pool as feasible.

Access to talent could be bolstered through reforms to the apprenticeship levy. Increasing industry access to apprenticeship levy funding, possibly combined with incentives for providing apprenticeships outside of London, could be beneficial.

International Partnerships & Trade

We welcome dialogue and cooperation between the UK and EU, and particularly the establishment of the UK-EU Financial Services Regulatory Forum. The Forum is an encouraging opportunity for strengthening regulatory cooperation on common issues such as accelerated settlement, Artificial Intelligence (AI) and improving the regional business environment in aid of economic growth.

---

[13] The City of London Corporation and EY (2024), *International talent and economic growth: Global competition and emerging trends*.

There are similar opportunities to strengthen financial services relationships with other jurisdictions, building fora such as the US-UK Financial Regulatory Working Group and mechanisms such as the Mutual Recognition Agreement (MRA) with Switzerland.

Developing a wider set of bilateral and multilateral ties offers the UK the opportunity to reduce friction and barriers to trade in global capital markets. This extends to deepening regulatory cooperation on common issues. For example, we would encourage the UK, EU and Switzerland to consider opportunities to coordinate their approaches to transitioning to T+1 both with one another and with APAC jurisdictions.

The UK asset management sector

We agree with HMT's assessment that the location of portfolio management activity is a pivotal part of the success of the UK's asset management sector, which in turn underpins the UK's strengths in wholesale services and trading.

With respect to opportunities in investment fund setup and administration, we agree HMT that developing a leading alternative investment funds offering, and developing a regulatory framework that fosters innovation – for example fund tokenisation solutions – are the right areas to focus.

Case study: Asset management in Scotland

Edinburgh has a long-standing reputation as the largest UK asset management hub outside of London. BlackRock has had a presence in Edinburgh since 1998. Analysis by the Investment Association notes that Scotland supports c. 13,000 jobs in investment management, as well as roles in the wider professional service ecosystem that support the industry such as such as custodian banks, transfer agents, wealth managers and legal advisors.[14]

The success of Scotland as both a regional hub for asset management and its continuing development as a globally competitive FinTech centre can be attributed to several factors that can serve as a template for regional growth:

- A long-standing history as an investment management centre, which developed alongside London's financial centre.
- Access to university spinouts and leading academic institutions committed to research and innovation.
- A national focus on reskilling and upskilling digital competencies which is helping the workforce adapt to rapidly evolving technology needs.
- The establishment of FinTech Scotland, a dedicated industry cluster organisation which has been crucial in catalysing growth.

FinTech Scotland, which is part of the FinTech National Network, was set up promote effective and purposeful collaboration between industry, academia and public sector. This has facilitated strategic partnerships that connect FinTech firms to education and innovation, financial service expertise, regulators, policy makers and Government to address shared challenges such as skills, talent, capital and investment.

[14] The Investment Association: *Investment Management in Scotland*

Facilitating technology and innovation

Jurisdictions around the world are embracing innovation to modernise financial market infrastructures, and improve the delivery and efficiency of financial services. It has been encouraging to see the UK signal its support for innovation and adoption of new technology.

Continuing to shape the future of the global financial system will require the UK to scale adoption of new, potentially transformative technologies. The creation of a network effect is vital here, since the more widespread digitisation efforts across the financial sector are, the more efficient and dynamic the capital markets ecosystem will become. It is absolutely right innovation should be balanced with carefully considered and appropriate regulation, but successful adoption of new technologies will also need to be tied to commercial benefits to incentivise widespread user adoption.

Distributed Ledger Technology, Digital and Tokenised Assets

Digitisation of assets (more commonly referred to as digital assets), tokenisation and the use of DLT are emerging as powerful transformative forces that can play a significant role in reducing fragmentation and removing structural silos that exist across traditional financial market infrastructure. Tokenisation of real-world assets could significantly improve the speed and coherence of capital market transactions and settlement processes, creating opportunities for pre- and post-trade efficiencies, increased transparency, and lower operating and investment costs.

Successful adoption of new technologies relies on several factors. While regulation is important, so too is the ability to create a network effect; this requires scalable Financial Market Infrastructure that brings together market participants across the full financial system and allows them to interoperate. For instance, we commend initiatives such as the recently-launched Digital Securities Sandbox (DSS), which allows firms to test products and services using DLT-based market infrastructures to create, trade and administer securities in a controlled and monitored setting, supervised by the BoE and the FCA.

Further to this, we also welcome HMT's commitment to launch a pilot tokenised digital Gilt using blockchain technology, and while activity in digital bond issuance has increased, we do however, remain concerned that institutional adoption will remain limited until infrastructure that can unify the full bond market ecosystem, including secondary market liquidity providers, financing, lending and collateral, is in place.

Perhaps most importantly, market participants need to be incentivised to adopt new technology and grow the digital network. One way to do this is to identify and remove existing structural micro barriers to entry. For instance, if the pool of eligible collateral acceptable to market participants included certain Money Market Funds, these could subsequently be tokenised – asset owners would then benefit from new forms of digital asset utility, operational efficiencies and potential commercial opportunities arising from new tokenised fund distribution networks, thereby increasing network participation. To this end, we have been supportive of the work undertaken by the Technology working group, a sub-group of the Asset Management Taskforce, which developed a blueprint for implementing fund tokenisation in the UK.

Artificial Intelligence

BlackRock considers digital disruption and artificial intelligence (AI) to be one of the mega forces shaping a new regime of macroeconomic activity and the future of finance.[15]

Many technologies such as traditional machine learning tools and techniques are not new and have long played a role in improving investment and portfolio management processes, trading and cybersecurity risk management.

However, the arrival of Generative AI has prompted a rapid expansion in the application of AI in the asset management industry. Generative AI has the potential to advance data analysis and pattern recognition beyond traditional machine learning capabilities. In addition to generating new insights, generative AI tools offer the potential to achieve more efficiencies in investment processes, allowing teams to focus on highest-value tasks. In trading, AI can help traders identify nuanced trading patterns, evaluate market scenarios, and assess liquidity provisioning and market impact. AI tools can also enable greater automation of basic trading tasks and augment decision-making. In cybersecurity risk management, AI improves threat detection and response capabilities, helping manage increasingly sophisticated and dynamic cyber threats.

The global regulatory landscape for AI is evolving rapidly, shaped by diverse policy priorities and geopolitical dynamics. Divergent AI policies have already become a reality, but different jurisdictions should avoid creating direct regulatory conflicts that could stifle innovation and create disparities among who beneficiaries of AI. For instance, the UK has sought to maintain its status as a global financial hub by pursuing a principles-based, sector-specific regulatory framework aimed at fostering innovation and attracting technology investments. The UK's framework for AI contrasts with the EU's centralized risk-based approach. It reflects diverging policymaker strategies that, while similarly aligned in prioritizing safety and accountability, may lead to fragmentation and compel the AI industry to operate based on jurisdictional preferences rather than work to reconcile different rules.

Supporting the UK FinTech sector

The UK FinTech sector can be supported through use of regulatory sandboxes, tailored regulations for emerging technologies, and streamlined licensing processes for fintech startups.

More broadly, the sector can be supported by the development of robust digital infrastructure, including high-speed internet connectivity and secure data transmission protocols; initiatives to expand access to basic financial services, promote digital literacy and awareness; strong cybersecurity standards; and collaboration and partnerships with international stakeholders to promote global interoperability is necessary to facilitate cross-border expansion for fintech companies.

Vibrant listed equity markets

Public equity markets are a critical part of a well-functioning capital markets ecosystem. Public market listings provide a source of permanent capital for businesses. They also play a role in enabling individual investors to contribute to and

[15] BlackRock: *Mega Forces: An investment opportunity*

benefit from the success of value-generating companies. With the Edinburgh and Mansion House Reforms, positive steps have been taken to reform the listings and public equity market. Below, we outline two areas that we believe can further bolster the UK's equity market activity.

Stamp Duty reform

The UK's Stamp Duty Reserve Tax is the highest tax-on-shares in the world. The transfer of standard equity shares in the UK is 0.5%, which is higher than that of France (0.3%), Spain (0.2%) and Italy (0.1%) while in the US and Germany there is no form of financial transaction tax. This serves as a deterrent to retail investors and pension funds investing more in the UK.

A way to reduce this burden could be to reduce financial transaction tax incrementally, with rates first reduced for some subsectors of the Financial Times Stock Exchange (FTSE), such as key industrial sectors such as life sciences and biotechnology companies. The reduction could then be extended more widely to target other sectors with a view to lowering the cost of raising equity while stimulating much needed retail savings and investment in the UK given the potential to positively influence investor behavior.

Development of a consolidated tape for equities and ETFs

Securities trading data is currently significantly fragmented, making difficult for investors to access an accurate picture of liquidity within the market. This can be addressed by developing a consolidated tape for both equities and fixed income.

Consolidated tapes are increasingly a fundamental building block of a modern financial market ecosystem, enhancing market competitiveness, transparency and resilience.

We commend the FCA's progress in developing a fully functioning consolidated tape for bonds by 2025. However, we remain concerned over the lack of progress to date made on developing a UK consolidated tape for equities and ETFs.

An appropriately constructed and well-designed consolidated tape that includes both pre- and post-trade data has the capability to increase investor confidence in secondary market trading activity: more information will be visible and transparent, making consumers of the tape aware of investment opportunities as they arise – thereby increasing competition and leading to better pricing and liquidity.

The EU is moving at pace to deliver its framework for a Consolidated Tape for both bonds and equities by 2025 and 2026/27 respectively; and the US stock market has had an equities tape since 1975 and a bond tape for over 20 years. We believe the UK needs to accelerate its progress to maintain its position as a modern capital market.